Exhibit A
Teitzel Affidavit
Attachment 1

BEST DEALS

Digital Telephone

COX Digital Telephone. Local Calling Areas

Exchange	Local Calling Areas
Bennington	Arlington, Blair, Ft. Calhoun, Fremont, Kennard, Louisville, Omaha (including Carter Lake, IA., Elkhorn, Gretna, Springfield, Valley, Waterloo), Yutan.
Elkhorn	Arlington, Blair, Ft. Calhoun, Fremont, Kennard, Louisville, Omaha (including Bennington, Carter Lake, IA., Gretna, Springfield, Valley,Waterloo), Yutan.
Gretna	Arlington, Blair, Ft. Calhoun, Fremont, Kennard, Louisville, Murray, Omaha (including Bennington, Carter Lake, IA., Elkhorn, Springfield, Valley, Waterloo), Plattsmouth, Yutan.
Omaha	Arlington, Bennington, Blair, Carter Lake, IA., Council Bluffs, IA. (including Carson, IA., Crescent, IA., Underwood, IA.), Elkhorn, Ft. Calhoun, Fremont, Glenwood, IA., Gretna, Kennard, Louisville, Macedonia, IA., Minden, IA., Mineola, IA., Missouri Valley, IA., Murray, Neola, IA., Oakland, IA., Plattsmouth, Silver City IA., Springfield, Tabor, IA., Treynor, IA., Yutan, Valley, Waterloo.
Valley	Arlington, Blair, Ft. Calhoun, Fremont, Kennard, Louisville, Omaha (including Bennington, Carter Lake, IA., Elkhorn, Gretna, Springfield, Waterloo), Yutan.
Waterloo	Arlington, Blair, Ft. Calhoun, Fremont, Kennard, Louisville, Omaha (including Bennington, Carter Lake, IA., Elkhorn, Gretna, Springfield, Valley), Yutan.
Carter Lake, IA	Council Bluffs, IA., Arlington, Bennington, Blair, Elkhorn, Fort Calhoun, Fremont, Gretna, Kennard, Louisville, Murray, Omaha, Plattsmouth, Springfield, Valley, Waterloo, Yutan
Council Bluffs, IA	Bethesda, IA., Brunsville, IA., Carson, IA., Carter Lake, IA., Crescent, IA., Glenwood, IA., Grant, Linn Grove IA., Macedonia, IA., Missouria, IA., Minden, IA., Mineola, IA., Missouri Valley, IA., Neola, IA., Oakland, IA., Omaha, Randolph, Rockwell City, IA., Silver City, IA., Sioux City IA., Treynor, IA., Underwood, IA.
Crescent, IA	Council Bluffs, IA., Mineola, IA., Omaha, Underwood, IA.

Exhibit A
Telcel Affidavit
Attachment 2

OMAHA METRO

COX COMMUNICATIONS

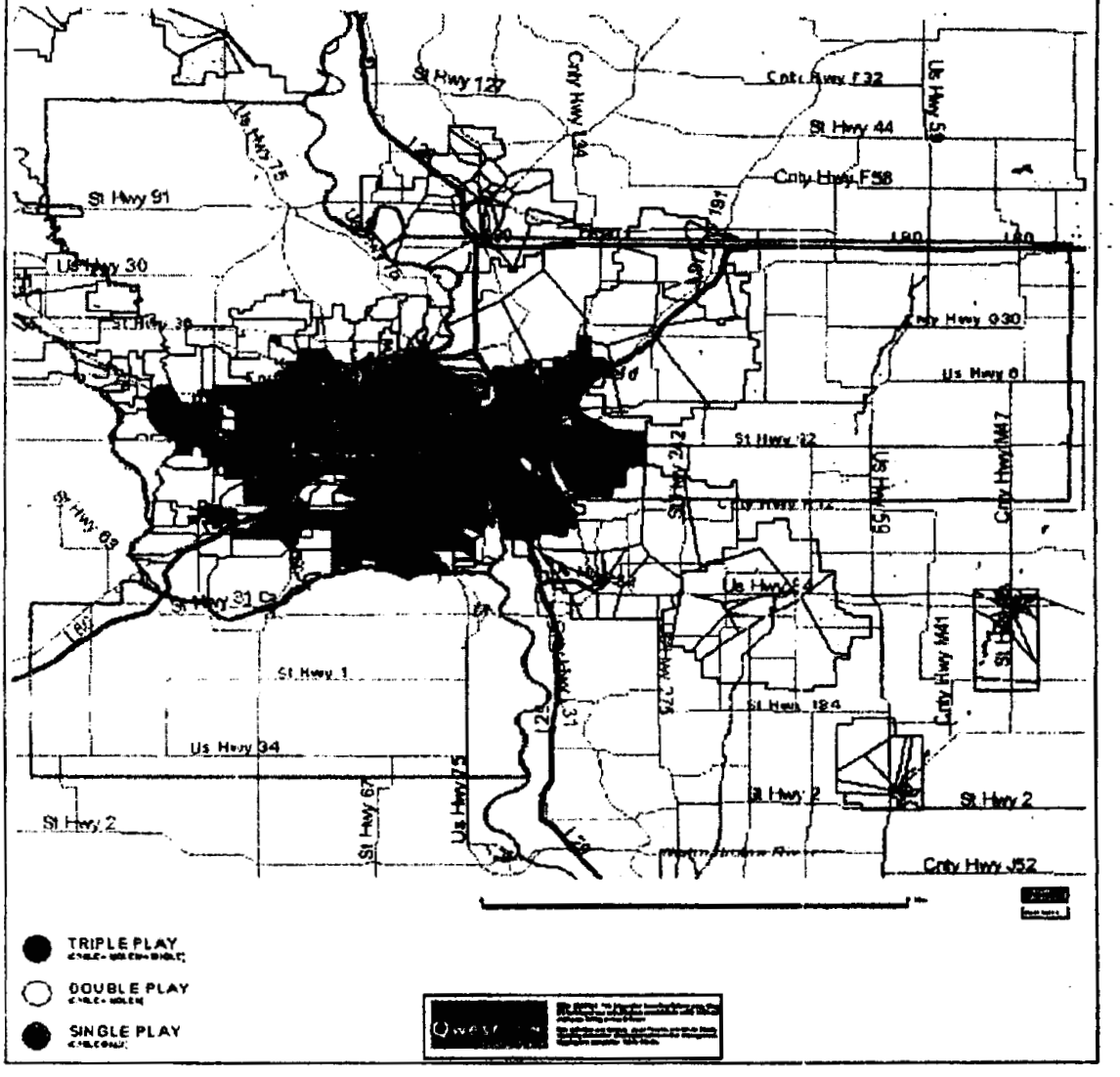
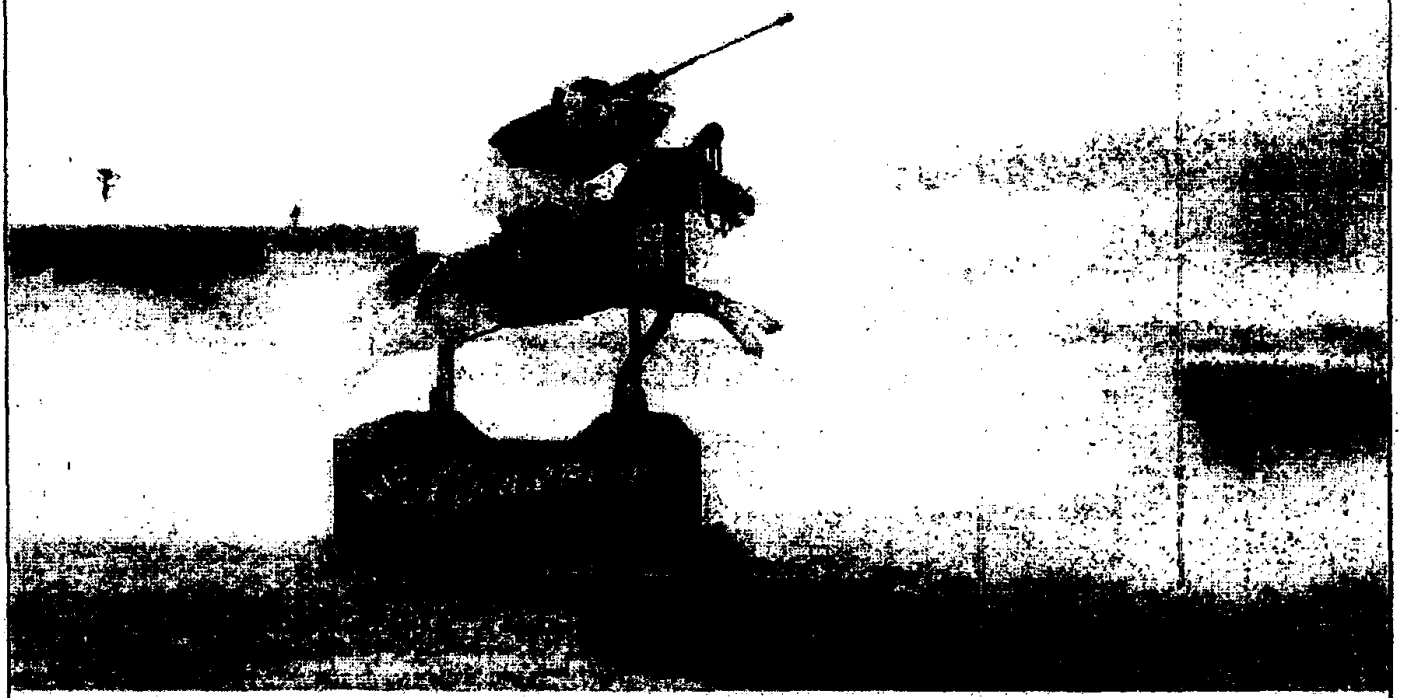


Exhibit A - Teitzel Affidavit - Attachment 3

TIRED OF DROPPING EXTRA MONEY INTO YOUR PHONE PROVIDER AND NOT GETTING ANYWHERE?



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Cox Commercial Cable keeps you up to speed on all the late-breaking news and information around the clock with more than 100 channel choices, plus a complete Music Choice option.

With our nationwide next-generation IP network, and 24/7 local technical support, you have all the horsepower and people-power you need to help you stay ahead of the competition.

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Exhibit A - Teitzel Affidavit - Attachment 4

COX COMMUNICATIONS

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Need password? Forgot password?

For Home | For Business | Order Services | View/Pay Bill | Customer Support | About Cox | Find service in your area Zip code

Omaha

Digital telephone

Bundle and save

Calling features

Price calculator savings

Special offers

BEST DEALS

EasyPay AUTOMATIC SECURE PAYMENTS

Digital Telephone

Description		Cox Communications	Qwest
Monthly Service - Line			
1st line	☑	$15.89	$18.15
Add a 2nd line	☐	$7.89	$16.35
Add a 3rd line		$15.89	$16.35
Add a 4th line		$15.89	$16.35
Monthly Service - Features			
Convenient Features			
Call Forwarding	☐	$2.90	$3.00
Call Waiting	☐	$4.90	$5.50
Speed Calling	☐	$1.90	$2.00
Three-Way Calling	☐	$3.40	$3.50
Voice Mail	☐	$5.90	$6.95
Enhanced Features			
Call Return - *69	☐	$2.90	$3.95
Busy Line Redial - *66	☐	$2.75	$3.50
Selective Call Forwarding	☐	$2.50	$3.50
Priority Ringing	☐	$2.75	$3.50
900/976 Restriction	☐	FREE	$1.00
Premium Features			
Caller ID	☐	$6.50	$6.95

Exhibit A - Teitzel Affidavit - Attachment 4

Caller ID	☐	[illegible]	[illegible]
Inside Wire Repair Coverage	☐	$1.50	$4.75
Initial Service Activation Charges			
Service Activation Fee	☑	$29.95	$33.00
Non-working Jacks Activated or Installed - Quantity: 0		$0.00 at $25/jack	$0.00 at $50/jack
Monthly total:		$15.89	$18.15
One time installation fees:		$29.95	$33.00

With Cox Communications, you'll save:
$2.26 a month, $27.12 a year!*

* The savings reflects Cox Preferred Rates (for customers who have at least one other Cox service). Pricing excludes tolls, taxes, and surcharges. Pricing for enhanced features does not include per use charges associated with some of those features, a more comprehensive desciption of pricing can be found in the pricing section of this site. Pricing and information valid only in the state of Nebraska. Rates subject to change. Services available only to residential telephone customers in Cox wired servicable locations, and all rates and saving comparisons exclude applicable taxes and surcharges and are subject to change. Individual savings may very based on services, location, and usage. Other restrictions apply. © 2002 Cox Communications, Inc. All rights reserved. Qwest rates effective as of 1/20/2002.

[illegible]

EXHIBIT B

Exhibit B - Redacted-for Public Inspection

STRATEGIC POLICY RESEARCH

AFFIDAVIT OF JOHN HARING, JEFFREY H. ROHLFS AND HARRY M. SHOOSHAN III*

JUNE 17, 2004

1. INTRODUCTION

In this affidavit, we explain the economic basis for our conclusion that Qwest should no longer be regulated as a "dominant firm" in the Omaha market for telecommunications services regulated by the FCC. We begin by explaining why we think the Commission's decision in this case possesses considerable policy significance, not just for the particular competitive issues raised by Qwest's petition for regulatory forbearance in a single, specific (and, as it happens, highly competitive) local operating environment, but also, importantly, for the conceptual coherence and integrity of the Commission's overall regulatory enterprise. If the Commission's regulations lose their connection to economic welfare (not to mention, economic reality) and continue to apply in competitive markets (*i.e.*, where there is no genuine market failure to be corrected), they run a significant risk of becoming increasingly intellectually "untethered" and economically arbitrary and capricious.

After describing the types of economic considerations that are relevant for an assessment of market dominance, we briefly summarize actual competitive conditions prevailing in the Omaha market and explain how these conditions are virtually completely at odds with those that must be found to prevail for a valid finding of economic dominance. Omaha thus presents a clear and compelling case where current FCC regulation is highly ill-matched to actual operating conditions, and where, in consequence, regulation has become "part of the problem" rather than "part of the solution." In our view, there is thus in this case a highly credible economic and public policy basis for granting Qwest's petition and sought-for, deregulatory relief.

* The authors are principals in Strategic Policy Research, Inc., an economics and public policy consultancy located in Bethesda, Maryland. Dr. Haring formerly served as Chief Economist of the Federal Communications Commission and Chief of the Commission's Office of Plans and Policy; Dr. Rohlfs was formerly Head of Economic Modeling Research at Bell Laboratories; Mr. Shooshan formerly served as Chief Counsel of the House Telecommunications Subcommittee.

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1.1. IMPORTANCE OF TIMELY REGULATORY RECOGNITION OF ACTUALLY PREVAILING MARKET CONDITIONS

In economic terms, regulation is conceived (in part)[1] in terms of offering a remedy for so-called "market failures" of different types (*viz.*, monopoly, externalities and neighborhood effects, adverse consequences derived from high transaction or information costs including under-provision of public goods, *etc.*) Regulation is itself not without either costs or potential failure modes of its own, so its adoption or maintenance as a remedy implies at least an implicit judgment that the (net) benefits (in terms of correcting market failures) are worth the costs (both direct and indirect) and any attendant adverse consequences (effects of "regulatory failures" akin to "market failures").

On this economic view, regulation is (or should be) an intellectually coherent response to a problem in economic organization that results in a potential opportunity for expansion of economic welfare through (regulatory) correction of a particular type of market failure (say, the exercise of market power). And on this view, the performance of regulation is gauged in terms of its efficiency in actually realizing such potential benefits. To the extent that regulation does *not* perform effectively and realize economic benefits and/or is not economically coherently conceived to address genuine market failures, it lacks conceptual legitimacy.

Making sure there is a close correspondence and good matching of "regulatory" means and "correction-of-market-failure" ends is critically important for (at least) two reasons. First, if there is not, "the (regulatory) cure may be worse than the (market-failure) disease," with the consequence that society is economically worse off from imposition or maintenance of ill-conceived and/or poorly implemented regulations.[2] Second, if the ends do not warrant the means and there is little perceivable connection between alleged problems and alleged regulatory remedies, the regulatory enterprise itself will be subverted as it is perceived to be increasingly arbitrary and capricious, lacking intellectual coherence and purpose as a carefully considered response to a genuine problem of economic organization.[3]

We think that, were there a genuine problem of market dominance and an authentically economically dominant firm existed, there could well exist grounds for regulatory intervention to

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[1] This is the "normative" view, in contrast to the "positive" or descriptive view which, somewhat more cynically, views regulation as simply another kind of economic "good" for which there is both a demand and a supply, and whose provision may or may not conduce to greater aggregate economic welfare in particular cases.

[2] Regulation's "killing the railroads" is an oft cited example: continuation of strict monopoly controls, long after effective competition in ground transport for the railroads (from trucks) removed the rationale for such controls, all but destroyed the railroads in the U.S. Deregulatory reforms in ground transport have more recently revived the railroads as both complementary and competing freight carriers with truck transport.

[3] ICC rate regulation of the *competitive* trucking industry is a good example of regulation in search of a "market-failure" rationale. The result in that case was subversion of regulation to anti-competitive ends. One would be hard pressed to find economists *defending* the ICC's regulation of the trucking industry as "efficiency-enhancing."

Exhibit B - Redacted-for Public Inspection

address this problem.[4] Because regulatory intervention often reflects the operation of other forces besides fulfilling the objective of addressing such problems, including, for example, private rent-seeking through effective pursuit of government favor, we would still wish to reserve judgment about the wisdom of particular regulatory interventions *in practice*, but we would certainly concede the *potential* efficiency of regulatory intervention is such circumstances.

Where we have more of a problem is whether—particularly in the actual circumstances currently prevailing in Omaha—there is, in fact, a problem of market dominance there to be addressed by regulation and whether Qwest is, in fact, a "dominant firm" as that term is usually understood in economics. The problem with *inaction* in the face of real change—an error of "omission," if you will—is that it *weakens* competition. The notion that competition should somehow be restrained in order to promote it is intellectually incoherent, not to mention a contradiction in terms.

1.2. COMPETITIVE BENEFITS OF TIMELY DEREGULATION

The "godfather" of economic deregulation, Alfred Kahn, has referred to a conundrum which he characterizes as the economic equivalent of "Catch 22": regulators typically do not wish to deregulate *until* there is effective competition, but they cannot know if competition is effective *unless and until* they deregulate. Trying simultaneously to run two regimes—one regulatory and one competitive—is liable to produce the worst rather than the best of both worlds. That is because competition tends to undermine regulation, while regulation tends to undermine competition.

One way in which the competitive process operates is through the pursuit of market advantage via invention and innovation of new products and service offerings. Indeed, on one highly significant view (that of Joseph Schumpeter), this is the most important aspect of competition from the standpoint of improving the lot of consumers.[5] Clearly one effect of the network "sharing" regulations attached to assignment of dominant-firm status in telecommunications is to stifle the regulated firm's incentives to engage in this highly "consequential" form of competition.[6] Indeed, it is precisely these disincentive effects that have led to the telling

---

[4] This presumes, for purposes of argument, that "real" economic dominance exists and that economically efficient regulation is the response adopted. In reality, dominance is a difficult premise to accept as even approximately realistic in today's telecommunications markets given the competition at hand. Moreover, that *current* regulation is itself economically efficient is a highly debatable proposition, which we would certainly question.

[5] Schumpeter's position was that such competition dwarfs the effects of competition "at the margins." *See Competition, Socialism and Democracy* (1950).

[6] *See* John Haring & Jeffrey Rohlfs, *The Disincentives for Broadband Deployment Afforded by the FCC's Unbundling Policies*, Prepared for the High Tech Coalition for submission before the FCC, *In the Matter of Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services,* CC Docket No. 001-37, April 4, 2002; and Haring & Rohlfs, *The Disincentives for ILEC Broadband Investment Afforded by Unbundling Requirements*, Prepared for the High Tech Broadband Coalition for submission before the FCC, *In the Matter of Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services*, CC Docket No. *(footnote continued)*

Exhibit B - Redacted-for Public Inspection

criticisms leveled against the "essential-facilities" doctrine in the legal and economic professional literature. Some "sharing" may be desirable, but sharing is by no means a "free good"—it is widely recognized to carry with it adverse consequences in terms of disincentive effects on investment: Why should firms invest if the benefits they are permitted to reap are limited by regulatory sharing arrangements?[7] One would not expect persons to invest in houses if ownership does not convey control of access; why would one expect profit-seeking (and capital-seeking) firms to behave any differently?

"Investment" does not always take the form of purchases of plant and equipment. Design and provision of information about new service offerings (say, packages of services that offer the transactional convenience of a "one-stop" shop) are also costly activities that entail substantial investments. But firms whose ability to reap advantages from such investments is attenuated by tariff-filing and advance-notice requirements will find less advantage in sinking funds in these kinds of activities. This has the consequence of reducing the vigor of the competitive process and the quality of service available to consumers. It may make the competitive life a "quiet life" (what English Economic Nobelist John R. Hicks characterized as "the best of all monopoly profits"), but that surely is not what policies touted as "pro-competitive" should be producing.

Where warranted, timely deregulation will thus allow competition to function more effectively and, in this manner, permit realization of public policy objectives in terms of a more competitive marketplace and realization of deregulatory reforms. To the extent regulation necessarily *distorts* the effective operation of a more thoroughly competitive process, it had better be doing so to some productive end. But where the market-power premise that supplies the putative motivation for regulatory intervention has ceased to exist, the costs borne as a consequence of allowing these distortions carry no off-setting benefits, at least for the consuming public.

Of course, in contrast to consumers, other *producer* interests may well stand to benefit from maintenance of unwarranted and counterproductive regulations. Indeed, the prospect of such benefits often supplies a powerful incentive for investments, *not* in better products and services, but in acquisition of governmental favor in the form of cartelizing regulatory management of competition and other forms of economically non-productive "rent seeking." In this instance, competition for government favor substitutes for marketplace competition on the merits. The way to prevent that from happening, or at least to minimize the harms associated therewith, is timely recognition of marketplace *realities*: when the anti-competitive harms of regulation likely exceed any pro-competitive benefits of regulation—because market dominance no longer exists and the reason for dominant-firm regulation has thus disappeared—the time to change policies is at hand.

001-37, July 16, 2002.

[7] Note that the fact that regulators may wish to "capture" such profits for redistribution to consumers via *other competitors* does not reduce the disincentive effect.

Exhibit B - Redacted for Public Inspection

We think that time has long come in Omaha, where it is difficult to see how any disinterested analyst could conclude that Qwest is the economically dominant operator. Before examining the circumstances currently prevailing in that locale, we provide a brief discussion of the economic meaning and appropriate application of the "dominant-firm" model of industrial organization economics. This will supply the relevant analytical context for discussion of Omaha specifics.

2. ECONOMIC MEANING OF MARKET DOMINANCE

2.1. UNILATERAL OR INDIVIDUAL MARKET POWER

In economic terms, the idea of "the dominant firm" has a specific and fairly straightforward meaning:[8] a dominant firm is one which faces such *weak* competition from actual and potential rival suppliers that it simply lets them "do their worst" and then searches for prices that maximize profits taking the "residual" demands (*i.e.*, the demands that are "left over" after rivals have taken *all they can*) as a given. As with the economic models of "perfect competition" or "perfect monopoly," the "dominant-firm" model produces "deterministic" results; less than perfect competition or monopoly, in contrast, produces analytical indeterminacies that require additional information about the specific manner in which firms are assumed to interact with one another in order to predict market outcomes.

Whether the "dominant-firm" model represents a good economic description of a particular marketplace depends on the realism and, hence, reasonability of assuming that the firm being analyzed (*viz.*, usually the so-called "incumbent" operator, although this is not entirely apposite when the local cable operator is one of the "other" competitors) can simply "afford" to let rivals do their worst and proceed blithely on its (and they on their largely inconsequential) way. That can presumably *only* be an accurate characterization of actual circumstances where the competitive damage rivals can inflict upon the incumbent is economically *minimal*. Where rivals can be credibly conjectured to do *a lot* of competitive damage, especially were the incumbent to (attempt to) exercise market power it does not possess or possesses only minimally, proceeding on the premise of an economically "dominant firm" represents an error and is, therefore, likely to produce flawed conclusions about appropriate regulatory policies.

The *actual or prospective productive capabilities* of competing suppliers determine the realism of assuming they pose a negligible threat to the incumbent's market hegemony: if competitive resource deployments and conditions of market entry are such that actual or potential competition of substantial magnitude is economically credible, it will be unrealistic and difficult to entertain such an assumption. It will be unrealistic for two reasons: (1) the actual and

[8] *See* John Haring and Kathleen Levitz, "What Makes the Dominant Firm Dominant?" Federal Communications Commission, Office of Plans and Policy Working Paper Series, Number 25, April 1989.

Exhibit B - Redacted-for Public Inspection

prospective market shares of rival firms will constrain and, indeed, plausibly render *counterproductive* any attempt by the incumbent operator to exercise market power by increasing the elasticity of market *supply*;[9] (2) the ability and willingness of consumers to switch to closely competitive substitute means to satisfy their preferences and requirements will similarly limit or preclude market power by increasing the elasticity of market *demand*.[10]

In the latter regard, it is worth pointing to the existence of so-called intermodal competition and its role in limiting market power and precluding market "dominance" in related sectors: thus, regardless of whether one regards wireless service as a sufficiently close substitute for wireline service to constitute the *same* economic good (*i.e.*, as trading in the *same* market),[11] the existence of good wireless service increases the elasticity of demand for wireline service and, consequently, the scope for any exercise of market power. One can (incorrectly in our own view) "exclude" wireless service from the relevant economic market, but so doing by no means renders wireless service irrelevant in assessing market power in a more narrowly construed "market" for wireline service. When wireless is "excluded," its effect still shows up in the measured elasticity of (narrowly-defined market) demand, which will/must be greater to the extent excluded services are at least somewhat substitutable for included ones (as is surely the case of wireless services with respect to wireline service).[12]

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[9] In economic terms, market power is defined as the ability to raise market prices and restrict market outputs *profitably*. The extant or impending capacity of rivals to take share limits the potential for profitable limitation of market supply. Rivals need not possess the ability to take *all* the business of their dominant rival; just enough to make monopolistic price increases unprofitable.

[10] No less an authority than Economic Nobelist Paul Samuelson has noted that:

> [T]he demand curve of any firm is equal to the demand curve of the industry minus the supply curve of the remaining firms, *already in the industry or potentially therein*. This being the case, it is easy to show that under uniform constant costs the demand curve for a firm is horizontal even though it produces 99.9 percent of all that is sold...Economically, if the firm were to begin to restrict output so as to gain monopoly profit, it would cease to sell 99.9 percent of the output or even anything at all. Consequently, it would not attempt to do so, but would find its maximum advantage in *behaving like a pure competitor*. (emphasis added)

See Foundations of Economic Analysis (1947) at 79.

[11] To be properly regarded as trading in the same relevant economic market, different goods and services need not be perfect substitutes for one another—there must simply be economically significant cross-elasticity of demand. All perfect substitutes trade in the same relevant markets, but *even* imperfect substitutes limit market power and dominance by increasing the elasticity of market demand and, hence, the scope for exercise of market power. Excluding a supply source from the relevant market on grounds of insufficiently high cross elasticity of demand does not imply that the availability of the excluded source does not operate to increase the elasticity of demand for supplies *within* the (narrowly-drawn) market—in fact, it does just that.

[12] This point is made explicitly by Judge Richard Posner & Professor William Landes in their famous *Harvard Law Review* article on "Market Power in Antitrust Cases" (94:5, March 1981). As they note (at 962):

> If the market were defined narrowly, the firm's market share would be larger [than if the market were

(footnote continued)

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So the *economic* issue in assessing market dominance is whether the firm being analyzed possesses *unilateral* (*i.e.*, individual) market power to restrict market outputs and raise market prices profitably. Characterization of a particular firm as economically "dominant" rests on the premise that the competition can capture only *minimal* share and, thus, that the dominant firm can safely let the competition "do its worst" and proceed virtually unharmed. The ability to take share turns on actual or potential productive supply capacity; if rivals possess substantial actual capacity and/or transparent ability readily to expand output from capacity already in place or to deploy additional productive capacity, the incumbent firm cannot "afford" to ignore the, in this case, assumedly *significant consequences* of any attempt to exercise market power and, therefore, cannot be accurately characterized as economically dominant.

2.2. EQUIVALENCE OF ECONOMIC AND LEGAL DEFINITIONS OF DOMINANCE

There is a clear and close correspondence between the economic meaning of market dominance and the applicability of the dominant-firm model to describe economic conditions in a particular relevant economic market, on the one hand, and the legal and regulatory administrative interpretations of the concept contained in the 1996 Telecommunications Act and those previously adopted by the Commission in related proceedings, on the other.[13] The latter have explicit reference to economic problems related to exercise of market power (*viz.*, "just and reasonable" rates, "protection" of consumers, pursuit of "public interest" objectives, *etc.*). Regulatory forbearance is specifically posited to turn on credible showings that regulation is not necessary to ensure just and reasonable conduct, to protect consumers or to promote the public interest.

The inapt characterization of a firm as economically dominant and the inapplicability of the dominant-firm model strongly suggest that regulatory arrangements premised on the reverse set of conditions will prove harmful.[14] Not only is dominant-firm regulation of a *non-dominant* firm *unnecessary* to ensure achievement of stated policy objectives, but it is also likely to *subvert* achievement of relevant objectives in terms of justice, reasonability, consumer protection and various public interests as have been specifically enumerated.[15] What may be appropriate *given*

> defined more broadly] but the effect on market power would be *offset* by the higher market elasticity of demand; when fewer substitutes are included in the market, *substitution of products outside the market is easier*. (emphasis added)

[13] *See Qwest Petition.*

[14] For example, Haring & Levitz (*op. cit.* at 8) state that "when no firm can be uniquely categorized as dominant, no asymmetric assignment of regulatory liabilities can be legitimately defended. A new market environment calls for new rules."

[15] *See supra* at 2 - 3.

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a genuinely dominant firm may well prove highly inappropriate in its absence. Indeed, the regulatory tools utilized to restrain the exercise of market power in one set of circumstances may well *promote* it in a different set of circumstances.[16] It is not a simple matter of redundancy, but rather of *counter*-productivity. And as we earlier argued, there are *also* important issues of *institutional integrity* implicated by a decision (or *in*decision) to maintain outmoded and intellectually incoherent "dominant-firm" regulations in the face of compelling contrary evidence.

3. QWEST'S NON-DOMINANCE AND ANOMALOUS REGULATED STATUS IN OMAHA

3.1. MARKET CONDITIONS DO NOT FAVOR EFFECTIVE OUTPUT RESTRICTION

Market power is the *sine qua non* for market dominance in the policy relevant sense.[17] Market power is, in turn, the ability to restrict *market* output and profitably raise *market* prices above the levels that would prevail in an environment where outputs could not be uneconomically restrained. The analytically relevant focus for diagnostic inquiry is thus on the basic conditions of supply and demand affecting the ability of a single seller to restrict output. Where, as in Omaha, prevailing conditions do not conduce to effective output restriction, the fundamental necessary requirement for economic dominance—unilateral market power—does not obtain.

The ability of one market participant to restrict market output obviously depends in a critical way on the ability of other market participants to expand output and thus to offset any output restriction. The ability to effect an offsetting expansion of output, in turn, depends on the ability of competing firms to enter a market and/or, having entered, to increase output either utilizing existing unused capacity or deploying additional productive capacity. The dual capacities to enter and increase relevant outputs thus turn on market "entry" conditions and whether there are any "binding" constraints on the availability of necessary resource inputs (including whether there is, in the short run, "excess" capacity available readily to increase the supply of desired outputs).

[16] Haring & Levitz (*op. cit.* at 17 and 18) observe that "effective recognition of mutual interdependence will be easier to the extent that tariffing and other regulations make it easier for competitors to signal their own intentions or to fathom the intentions of their rivals," and that "the public might well be harmed if new regulation actually facilitated collusion."

[17] A firm that "dominates" its market in consequence of the excellence of its performance in competition with its rival competitors does not present a market-failure problem for public policy to address.

Exhibit B - Redacted-for Public Inspection

With respect to the existence of barriers to output expansion in the instant setting, we would note, first, that there are no legal barriers preventing expansion of output by competitors; indeed, a principal thrust of post-1996 Telecom Act policy has been systematic removal of virtually all such barriers and implementation of a variety of policies designed to facilitate easy entry. It is important to remark in this regard that the State of Nebraska *has long been in the forefront* of pro-competitive *de*regulatory reform; open markets and (comparatively) free competition have been the rule there *since 1986.* Not surprisingly, competition (and, primarily, "facilities-based" competition at that) has thrived there and the State's innovative policies are widely viewed as a virtually unqualified success. The consequence in Omaha has been competitive entry in a wide variety of shapes and forms, including *facilities-based* entry utilizing both conventional (wireline) and unconventional (wireless, VoIP) technologies and riding on standalone (wireless, wireline) and shared technology platforms (cable), as well as *resale-based* entry utilizing both discounted retail services and bundled network elements (UNE-P).

The equipment required to provision and implement an expansion of output is, for the most part, produced under conditions of constant or increasing returns to scale. The relevant technological "know-how," while itself specialized, is not so limited in supply (and "superior" as, say, Saudi oil reserves) as to inhibit economic expansion of output.[18] Given the depressed state of the communications equipment supply industry, equipment suppliers would presumably be only "too happy" to facilitate further expansion of communications service outputs through sales of new capital equipment and consumer gear.

Economies of scale are sometimes cited as potential barriers to expansion of output and competition in telecommunications markets. Two general points are worth noting in this regard. First, not all technologies capable of meeting consumer demands are characterized by the *same degree* of scale economies and some also possess potentially offsetting economies of *scope* that may facilitate competitive entry. Thus, it is clearly feasible to exploit technologies that are capable of providing a *variety* of services (*e.g.,* multi-channel video program delivery or electrical power distribution in addition to telephony services—whether POTS or high-speed Internet access)[19] so that more applications can "ride" on any necessary dedicated or share facilities including rights of way. Alternatively, technologies that involve less, perhaps only minimal, utilization of "dedicated facilities" (such as fixed access lines "dedicated" to particular users)—wireless is an example—may also be economically exploited.

In these regards, consider that, in the case of cable, while individual consumer "subscriber lines" are required (*i.e.*, a "dedicated" subscriber "access" network is necessary),[20] to deliver service,

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[18] George J. Stigler cites the existence of "superior resources" as "occasionally" and usually only "temporarily" creating and permitting the exercise of some market power. *See The Theory of Price* (New York, Macmillan, 1966).

[19] Of course, there is also clearly considerable scope for economies in joint provision of various telecommunications services themselves, say, high-speed broadband access services and VoIP telephone calling, for example.

[20] There is, of course, a lot of resource "sharing" involved in the provision of cable's various supply offerings *among different consumers* as well (*cf.* video programming inputs).

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much of this capital infrastructure can be utilized to deliver *several* different services (including, in the first instance, multi-channel video programming and, in addition, high-speed Internet access, POTS, VoIP and various home management services), so costs can be effectively spread over many different kinds of outputs (*i.e.*, there are considerable economies of scope). Thus, the cable industry can, and, indeed, has (as we shall presently remark in Omaha) manifestly overcome this potential "barrier" to delivery of phone service, and there is nothing preventing a further expansion of service to whatever degree is demanded in the (local) marketplace. Indeed, there is a forceful economic (*viz.*, profit) dynamic pushing such expansion.

With wireless services, the story is a little different; entry via this means is economically feasible and plainly not precluded or blockaded by economies of scale (and, again, has already occurred, seemingly rendering the issue of entry feasibility somewhat academic)—in this case because the degree of feasible network resource sharing is greater than with wireline service (*i.e.*, a smaller percentage of the relevant assets are "dedicated" to individual users/a larger percentage of productive assets are "shared").

The second point that it is important to note, in terms of the comparative economic *in*significance of scale economies and opportunities for competition, is that *voluntary contractual* sharing of network facilities is an entirely feasible alternative, implying ample opportunities to share in economies from resource-sharing. Indeed, there are, as we shall presently describe, powerful economic and strategic incentives pushing toward effective exploitation of opportunities for realizing cost economies through network-resource sharing. The great debates about the economically appropriate extent of network element unbundling and whether a second "resale window" is appropriate are primarily debates about appropriate contractual terms and conditions and appropriate means for determining them. These debates and the commentary associated with commercial bargaining negotiations (especially that disclosed/advertised in public) should not be allowed to obscure the fundamental economic realities working in favor of "deals" being struck—in particular, the economic cost savings that potentially inhere is network sharing arrangements.[21]

To what extent should transactions occur at mutually advantageous terms defined by the preferences of buyers and sellers, as with most marketplace exchanges, and/or to what extent should they be conditioned by governmental constraints and compulsion? In the absence of the latter, terms and conditions may well vary (from those currently prevailing—but under legal duress), but that, by no stretch, *precludes* deals being cut; indeed, the absence of constraints and compulsion may well permit realization of very attractive transactions for capabilities that would

[21] The incentives of both buyers and sellers are complex: of course, buyers would like to pay less, but they would also like to buy more; and while sellers would like to charge more, they would also like to sell more. In both cases, there are thus *internal* as well as external conflicts to be reconciled.

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otherwise not be economic to undertake or only undertaken on much less favorable and attractive terms.[22]

3.2. STATUS OF COMPETITION IN OMAHA

As we have seen, "what makes the dominant firm dominant" is the conjectured *inability* of competing firms to make economically significant competitive inroads against the dominant firm. A real dominant firm faces such *weak* competition that it can simply allow the competition to do what(ever) it will, since *by assumption* (if the "dominant-firm" model is an accurate depiction) this amounts to very little, and then proceed to optimize its economic decisions with respect to the demand that remains—*i.e.*, the "lion's share" of demand *given* the premise of *weak competition.* A firm is thus dominant less because it is strong than that the competition it faces is weak—alternatively, it is strong/dominant *because* the competition is weak.

Turning to the specifics of competitive conditions actually prevailing in Omaha, one is immediately struck by the transparent *inapplicability* of this analytical model as a means to describe Qwest's ostensible competitive status and *modus operandi* in this market. Far from confronting weak competition that can, even potentially, inflict only minimal competitive harm, Qwest confronts competitors that have *already* taken a substantial/indeed, a "lion's" share of the business, and are evidently—given the productive capacity they have *already* deployed—fully capable of taking even more and, moreover, possessing compelling economic incentives (given the productive capacity that has already been sunk) to do so. For Qwest, it is thus hardly a matter of allowing "scavenging" rivals to share a little of the competitive "catch," given their ability to take *only* a little; it is instead a matter of Qwest *itself* needing to (be *free* to) strive vigorously to retain sufficient business to remain competitively viable.

In his affidavit,[23] David L. Teitzel has developed market share estimates for residential and business local exchange service in the Omaha MSA. It is worth noting that, while Teitzel's estimates are *inconsistent* with economic dominance by Qwest, they are, nevertheless, analytically quite *conservative* measures, *i.e.*, if anything, they are likely to *overstate* Qwest's degree of economic "dominance," since they "exclude" economically significant intermodal demand substitutes (*viz.*, notably wireless and rapidly growing VoIP services).[24] As we observed above, the competitive effect of excluding demand substitutes from the economically "relevant market" (on grounds of insufficiently "close" substitutability to warrant inclusion in the "same" market) must necessarily manifest itself in a *higher* market demand elasticity implying *less* potential scope and incentive for any exercise of market power. In order for excluded services to

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[22] Recall the proverbial tale of the heavily discounted can of tuna fish, whose only disability is that there is none to be found on the grocer's shelf.

[23] *See Affidavit of David L. Teitzel, Local Telecommunications Competitive Environment: Omaha/Council Bluffs,* dtd.

[24] Because they are conservatively based and fail to reflect certain relevant forms of competition, Teitzel's market share estimates *understate* Qwest's *non*-dominance.

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have *no* impact on the (relevant) market demand elasticity (and the degree of market power), one would have to assume, rather drastically and surely unrealistically, that there would be *no* substitution toward excluded services were relative prices to change and given other service characteristics besides relative prices affecting the "value-for-money" proposition confronting consumers in particular circumstances.[25]

Teitzel estimates that CLECs now account *for more than* [redacted] *percent* of the Omaha market denominated in access lines.[26] By far the bulk of these lines reflect "facilities-based" competitive alternatives with only about [redacted] of some [redacted] thousand total lines supplied through offerings derived from the two "resale windows" (UNE-P and resold retail lines).[27] Moreover, the bulk of the competition's gains have come out of Qwest's "hide" rather than market growth—Qwest's access baseline has declined by *more than* [redacted] *percent* since year end 2,000 through February of this year. Qwest has lost more than [redacted] residence lines and more than [redacted] business lines over this period. The customers Qwest has *lost* are amongst its *most valuable* ones, accounting for the highest consumption values and a disproportionate share of the calling.

An ostensibly "dominant" firm that loses [redacted] of its business over a three-year period and finds itself with a *declining* market share of *less than* [redacted] percent can, by only the most difficult and implausible of intellectual stretches, be categorized as economically "dominant"—"desperate" or "driven" strike as perhaps more apposite adjectives in these circumstances. This is particularly so given the specific identities of the competitors Qwest confronts in the Omaha market, the productive facilities these competitors have *already* deployed and the economic imperatives plainly dictated by these various resource deployments.

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[25] One may wish to define markets narrowly for any number of reasons (some good/some bad), but "squeezing the balloon" in this fashion does not *moot* the competitive impact of the excluded substitute's existence; it merely leads to its competitive manifestation on the demand side rather than in a lower measured market share on the supply side (*i.e.*, in terms of the market's necessarily *greater* demand elasticity and resultant lesser susceptibility to monopolistic exploitation). Growth in demand for wireless and VoIP services in significant part represents substitution for less *economical* wireline calling. In the case of wireline-versus-wireless calls, this stems from the frequent effect of convenience/inconvenience which often makes a wireless call more economic notwithstanding a (sometimes) higher price. Heretofore, VoIP has primarily afforded international callers with an economic alternative to often highly inflated charges for such calls, notwithstanding lower technical call quality. With rapid technical advance, the latter disabilities of VoIP are rapidly becoming a thing of the past.

[26] CLECs are estimated to supply [redacted] percent of the total number of lines ([redacted] percent of residence lines and [redacted] percent of business lines). Consumers who avail themselves of competitive alternatives are typically heavier callers, implying that CLECs now account for an even higher proportion of calling in Omaha.

[27] We believe it is worth stressing the extent of *facilities-based competition* in the Omaha market: UNE-P accounts for only a very small part of the total competitive picture there, and its subsequent disposition is a matter of comparatively little import for assessment of competitive conditions there. Nevertheless, as we presently note, there is every reason to expect continued competitive activity utilizing this type of input provisioning based on mutually advantageous gains from trade.

It is worth noting, by way of comparison, that Qwest has lost *greater* share in the Omaha market than AT&T had in the national market for long-distance service at the time the FCC declared it non-dominant.[28] Indeed, Qwest's Omaha operation has not only lost share *in relative terms*, but has also suffered losses of business *in absolute terms*. AT&T, in contrast, while suffering significant share losses in long-distance was still able to grow its business in absolute terms, given increases in the size of the long-distance market (*i.e.*, market growth) during the applicable period. In both cases, significant share losses were manifest as was the deployment of significant competitive productive capacity.

In Omaha Qwest is not exactly being "eaten by ants" (not that it is impossible to be "eaten by ants" in an economic manner of speaking; *cf.* United and American Airlines and their losses to small discount airlines generally offering "point-to-point" service rather than running "hub-and-spoke" networks).[29] Qwest's most significant competitor in the Omaha MSA is Cox, one of the nation's leading cable MSOs. In addition, facilities-based local exchange service offerings are being made by McLeod, Alltel and Huntel, each a significant enterprise with telecommunications operations and experience in a multitude of competitive venues.

Teitzel utilizes changes over time in the number of Local Interconnection Service (LIS) trunks in service within the market to gauge the growth of competition and to estimate the growth of the access lines served by facilities-based CLECs.[30] He finds that the number of such trunks used by facilities-based CLECs in Omaha *has approximately doubled* since December 2000 as CLECs have resized their networks to accommodate a rapidly growing customer base. Again, this is an observation that is virtually impossible to reconcile with market "dominance" by Qwest.

Teitzel also examines information contained in the Local Exchange Routing Guide (LERG) that describes, *inter alia*, the local switches deployed by carriers within a state, the area codes and prefixes assigned to each switch, the rate centers served, the types of switches deployed, their physical location and other types of information of use in ensuring efficient processing of calls in a "network of networks." He finds eight CLECs with prefixes assigned to switches serving rate centers in the Omaha-Council Bluffs MSA. Not all carriers list the specific identity of the switches they have deployed, sometimes simply noting, for example, that a "digital switching system" has been installed. Several switches are specifically identified, and Teitzel remarks that

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[28] *See* John Haring, Jeffrey H. Rohlfs and Harry M. Shooshan III. *Disabilities of Continued Asymmetric Regulation of AT&T.* Prepared on behalf of AT&T for submission before the FCC, *In the Matter of Motion for Reclassification of AT&T as a Nondominant Interexchange Carrier,* CC Docket No. 79-252 (June 30, 1995).

[29] Indeed, "death by a thousand cuts" may be a less preferred way of going. The "dominant-firm" model can potentially be utilized to analyze cases where the so-called "competitive fringe" is large, as long as no single firm is so large that the dominant firm must take its potential competitive responses into account. That is decidedly *not* the case with regards to Qwest's position in Omaha in relation to Cox and the several facilities-based CLECs in confronts in contesting for the custom of *both* residence *and* business customers.

[30] As Teitzel notes (at 5), as the number of end-user lines served increases, the number of LIS trunks in service must also increase to minimize call blockage.

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three of the Omaha CLEC switches *alone* possess sufficient capacity to accommodate some *400 thousand* end-user lines—more than *double* the number of CLEC lines estimated to be "in service" currently and more than [redacted] percent of the *total* number of lines currently in service.

These data indicate that there is ample "excess" switching capacity *currently deployed*, and that competitors are well-positioned to expand the number of access lines they serve.[31] These data are completely inconsistent with "weak" competitors incapable of inflicting significant competitive losses on Qwest. To the contrary, competitors are in a position to take virtually *the whole market* (more than [redacted] of which they have already taken)—hardly a condition conducive to sound sleeping let alone allowing rivals to take their fill *for what does it matter!*

Switches are obviously not the only form of capital from which expansion not only *can* emanate, but is also presumptively *compelled* by competition and profit-seeking behavior. For example, we earlier noted the existence of significant potential economies of *scope* derivable through more intensive utilization of existing plant and equipment. A cable-system operator can use "subscriber lines" not only to deliver video programming, but also to supply telephone services, high-speed Internet service and so on. Indeed, a prime current competitive marketplace "modality" is to offer a "one-stop shop"—a transactionally convenient bundle of services.

Indeed, to the extent this type of *extensively* bundled type of offering is what consumers, by and large, desire, the cable operator in any given locality would appear to possess some significant competitive advantages, certainly relative to the traditional telephone company. It can, for example, use its network to supply a ubiquitous high-speed Internet access service (in contrast to telco-provisioned DSL which suffers geographical impairment) and to offer a very large menu of different types of video offerings. It thus has more ways "to skin the cat," in particular, more potential revenue streams to tap more economically in recovering the costs of its network investment.[32] Consumer "tastes & preferences" are what define economically relevant "product" markets. If consumers largely seek an extensive bundle of services—and view such a bundle as "superior" to a disaggregated set of offerings—the vendor who can most efficiently assemble such a bundle has an economic advantage. Whether such an advantage translates to "dominance" is an open question; what does seem abundantly clear is that a "plain, old telephone company" can hardly be considered the dominant player in this new kind of game.[33]

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[31] This is not to imply that such expansion may not require plant upgrades of various sorts to facilitate growth. For example, to offer cable modem service throughout its entire local network, Cox may need to upgrade its fiber facilities. Teitzel remarks that Cox is currently advertising its *full* service package *extensively* throughout the core market in Omaha.

[32] Not only does the cable operator possess a larger bundle of potential offerings, but if there are economies of internal organization (versus integration via, say, contract), the cable operator will be able to exploit these multiple revenue streams at lower effective costs.

[33] Where continued regulation is deemed appropriate (say, with respect to charges for terminating access), there is no economic basis for treating Qwest's access charges any differently *in regulatory terms* than Cox's or the other CLECs' rates. It is the "character" of termination not the specific identity of any particular carrier that conceivably
(footnote continued)

3.3. VERY HIGH IMPLIED ELASTICITY OF DEMAND FOR QWEST SERVICE

The elasticity measure relevant for assessment of a firm's market power is the price elasticity of demand *it* (*viz.*, the firm) confronts—as opposed to the market elasticity of demand. While a high market demand elasticity precludes a low firm elasticity, a *low* market demand elasticity by no means precludes a *high* firm elasticity. Indeed, individual firm elasticities of demand, in general, are much greater than market demand elasticities.[34] That is because while consumers may lack close or perfect substitutes *outside* any given relevant market, making the *market* demand less than perfectly elastic,[35] they usually have, at least, some alternatives (other than the case of "pure monopoly") within any given market and there is, generally, some non-negligible prospect of entry or expansion of output from productive capacity already deployed, further increasing demand elasticities perceived by individual firms.

Market demand elasticities for telecommunications services are often estimated to be relatively price inelastic or unitary elastic.[36] Individual firm elasticities are much higher because these reflect consumers' ability to switch to competitors' offerings in the event of a price increase by one supplier. In the Omaha market, the service demand elasticities perceived by Qwest are quite *high*—*i.e.*, demand is very *elastic*, indeed. Consider that with several firms offering virtually indistinguishable service offerings to Qwest's telecommunications offerings at comparable, competitive prices, any attempt by Qwest to raise the prices of its offerings would prompt wholesale substitution of its competitors' offerings by consumers.

Indeed, within a comparatively short period of time, the mere *introduction* of competitive offerings into the Omaha market at modestly discounted prices and as part of discounted "bundled" service offerings (in one notable instance, *extensively* bundled to include MVPD service from cable) has produced very substantial business losses for Qwest. The observed *fact* that Qwest's market share has *more than halved* within three years in response to *far less* than an effective halving of prices is consistent with a *very elastic* demand for Qwest's service.[37]

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triggers a regulatory requirement in this type of case.

[34] Even in the case of a pure monopoly, where the elasticity of demand for the firm's outputs and market output are seemingly the same, the potential for entry in response to a price change likely renders the perceived firm elasticity greater than that of the market.

[35] As earlier noted, less-than-perfect substitutes—which *are*, nevertheless, *partial* substitutes—*do* increase market demand elasticities, but their "imperfection" is precisely what "defines" an economically relevant market. Economically relevant markets are often defined as "chinks in the chain" of substitutes.

[36] With a unitary elastic demand, a small percentage price change prompts an equivalent percentage change in quantities demanded.

[37] Price elasticities are, of course, formally defined in economic terms in "instantaneous" terms, *i.e.*, for percentage price changes posited to be arbitrarily/infinitely small, with other relevant factors held constant. The facts actually observed in Omaha over the last few years imply that, could one measure the relevant elasticity directly, it would be
(footnote continued)

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Highly elastic demands, in turn, preclude any opportunities for *profitable* restriction of output. Not only is Qwest plainly not in a position to restrict *market* output, given the supply capabilities of its actual and potential rivals, their ready availability as a demand substitute for Qwest's offerings—an alternative consumers have plainly shown themselves fully willing to exploit—implies that Qwest has no ability to raise market prices in a non-competitive manner.

4. CONCLUSIONS

Strictly speaking, economic dominance entails the ability not only to restrict market output and raise market price, but also, and importantly, by *inconsequential effects* of so doing on the competitive behavior and effectiveness of actual and potential rival firms. If the exercise of alleged "dominance" is merely to afford profitable and promptly realizable expansion opportunities by rival firms, there is no economically meaningful sense in which dominance can be posited to exist. Dominance requires an absence of competitive productive capacity and binding constraints on expansion of such capacity. Neither of these conditions can accurately be said to characterize the Omaha market. Quite to the contrary, competitors there have *already* made very substantial competitive inroads and appear to possess ample capacity and a great likelihood of making further ground on the incumbent telephone company; indeed, any attempt by Qwest to exercise "dominance" would be entirely self-defeating and economically irrational in the prevailing circumstances.

It is incontrovertibly the case that operating realities in Omaha strongly support Qwest's lack of market dominance and it petition for relief from FCC regulation as a "dominant firm" in this market. Not only is deregulatory relief strongly warranted in this case, but there is a substantial basis for thinking that the sought-for relief will promote *more vigorous competition.* By the same token, it would be a failure to grant relief that would inhibit competition and, thus, be fundamentally at odds with achievement of public-policy objectives in terms of promotion of competition, consumer welfare and the public interest. Maintenance of unnecessary and ill-adapted regulations would conflict with achievement of sought-for objectives, and would also produce a highly undesirable side effect: it would subvert the basic legitimacy and integrity of the regulatory undertaking and undermine support for the regulatory enterprise where its operation may well be justified.

In our view, granting Qwest's petition would allow the FCC to "do the right thing" and compellingly demonstrate both its commitment to real competition and its ability to function as an "honest broker."

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much greater than unitary elastic, *i.e.*, very elastic.

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CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify that I have caused the foregoing **PETITION (redacted) OF QWEST CORPORATION FOR FORBEARANCE PURSUANT TO 47 U.S.C. § 160(c)** to be 1) filed with the Office of the Secretary of the FCC and 2) served, via hand delivery, on the FCC's duplicating contractor, Best Copy and Printing, Inc., at the following addresses:

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Office of the Secretary
Federal Communications Commission
Room TW-A325
445 12th Street, S.W.
Washington, DC 20554

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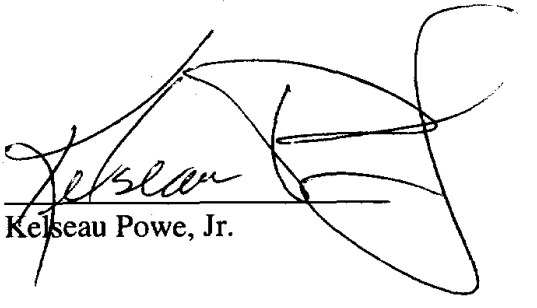

Kelseau Powe, Jr.

June 21, 2004